

Sovereign Resilience: The Investment Imperative

- Sovereign resilience and defense investment are becoming imperative as geopolitical risks escalate.
- U.S. defense policy uncertainty contrasts with Europe's strategic awakening, driving divergence in global defense markets.
- European defense equities are outperforming, reflecting confidence in sustained government spending and supply chain localization.
- Geopolitical catalysts, including Ukraine and China, are accelerating defense modernization and independent procurement strategies.
- Next-generation defense technologies, such as AI, cybersecurity, and autonomous systems, are gaining priority, shifting procurement away from traditional primes.
- Private capital is playing a growing role in funding defense innovation as governments seek faster, more agile procurement solutions.
- BOKA Capital is well-positioned to invest in deep technology companies driving the next wave of defense transformation.

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Executive Summary

The past several weeks have underscored the fundamental shift underway in global defense policy and investment. Across both sides of the Atlantic, national security and sovereign resilience have re-emerged as central economic and political priorities. Rising geopolitical tension in Ukraine, uncertainty around U.S. defense funding, and Europe's accelerating rearmament reconfirmed defense technology as a key investment area of the next decade.

Public markets have begun to reflect these shifts. While European defense equities have seen a significant rally in response to increased government spending commitments, U.S. defense primes have faced valuation pressure amid uncertainty around procurement priorities. The broader implications extend far beyond listed equities. Governments are now prioritizing long-term investments in emerging defense technologies, supply chain resilience, and industrial base modernization – trends that are reshaping capital allocation across the sector. As these structural changes unfold, private capital will play a pivotal role in advancing next-generation defense capabilities, positioning investors with exposure to this transformation at the center of a multi-year investment cycle.

“The future of defense lies in technological superiority, and private capital will be essential in driving the next generation of innovation to safeguard sovereign resilience.”

– Sir Ben Wallace, Partner, BOKA Capital

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Over the past several weeks, global defense policy and investment dynamics have entered a new phase of acceleration. Key developments across the U.S. and Europe underscore the growing importance of sovereign resilience, supply chain security, and next-generation defense technologies.

1. Policy Realignment: U.S. Uncertainty vs. Europe's Strategic Awakening

The U.S. defense sector is experiencing a period of transition, marked by budgetary constraints and political shifts that are influencing procurement priorities. The Department of Government Efficiency (DOGE) initiative has introduced short-term uncertainty, with proposals for an 8% reduction in the FY26 defense budget, amounting to a \$50 billion contraction. The administration has emphasized continued funding for missile defense, nuclear deterrence, and autonomous systems. In fact, President Trump's recent address to Congress outlined plans to create "the most powerful military of the future" while prioritizing U.S. domestic defense production. A key component of this agenda is the proposed "Golden Dome," a next-generation missile defense system designed to protect the U.S. homeland from aerial and missile threats. This initiative is expected to generate significant opportunities for U.S. defense primes, particularly in missile interception, space-based defense architecture, and propulsion technology. Nevertheless, traditional procurement categories face increased scrutiny. Compounding the challenge, recent discussions around fiscal policy suggest that the Pentagon will be required to operate within stricter cost controls, adding further complexity to long-term planning.

The impact of these developments is already visible in equity markets. U.S. defense primes – including Lockheed and General Dynamics – have declined up to 7% year-to-date, reflecting investor concerns over procurement reprioritization. The market has responded negatively to the lack of budget clarity, despite robust order books and continued geopolitical risk factors.

In stark contrast, Europe has entered a period of accelerated defense investment, driven by a growing recognition that security cannot remain dependent on U.S. commitments. The European Commission recently announced a special defense funding package aimed at strengthening local supply chains and reducing reliance on non-European contractors. Germany has taken the most decisive step, unveiling a €500 billion infrastructure and defense fund, which

will be exempt from constitutional debt constraints. At the Munich Security Conference, both European and U.S. leaders reinforced the expectation that NATO allies will increase defense spending well beyond the 2% GDP baseline, with targets now shifting toward 2.5-3%.

2. Public Market Divergence: U.S. vs. European Defense Equities

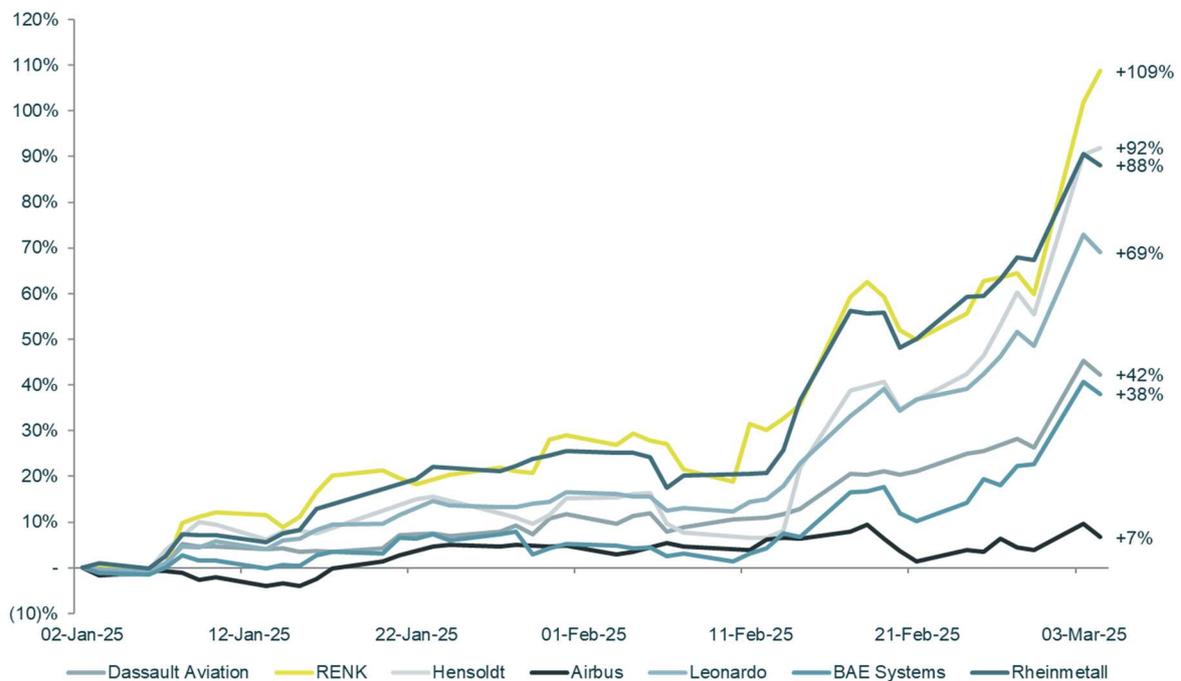
The stark divergence in defense stock performance over recent months reflects broader market expectations regarding the trajectory of defense spending. European defense stocks have rallied significantly, as investors anticipate sustained government investment. Shares of RENK (+109% YTD), Hensoldt (+92% YTD), Rheinmetall (+88% YTD), Leonardo (+69% YTD), Dassault Aviation (+42% YTD), and BAE Systems (+38% YTD) have all experienced notable gains, driven by expectations of long-term procurement demand. The re-rating suggests that the market views the increase in defense spending as a structural change rather than a cyclical trend.

Conversely, the underperformance of U.S. defense primes highlights investor uncertainty regarding future procurement cycles. Lockheed Martin has declined 7% YTD and General Dynamics is down 4%, despite a continued strong backlog. Instead, the lack of clarity around the Pentagon’s spending priorities has weighed on sentiment, leading to a compression in valuation multiples. U.S. primes¹ are currently trading at an average forward P/E of 18.4x. Meanwhile, European defense stocks² are trading at 25.4x, reflecting increased confidence in long-term defense spending commitments.

This valuation gap does not change the fundamental reality that global defense spending is increasing. This valuation divergence highlights the fact that while US defense spending has historically been – and remains – robust, European defense investment has reached an inflection point, underscoring the region's significant need to catch up. Governments remain committed to modernizing military capabilities, and private capital is positioned to play a crucial role in financing and developing next-generation defense solutions.

YTD Share Price Development of European Defense Stocks³

% Share Price Performance



¹ RTX, Lockheed Martin, Northrop Grumman, L3 Harris, General Dynamics.
² Rheinmetall, BAE Systems, Leonardo, Airbus, Hensoldt, RENK, Dassault Aviation.
³ Source: PitchBook as of 04-Mar-2025.

3. Geopolitical Catalysts: Ukraine, China, and the Broader Strategic Landscape

Beyond budgetary factors, geopolitical risk remains elevated, reinforcing the long-term need for defense investment. The conflict in Ukraine, which has long relied on Western military assistance, has entered a new phase of uncertainty following the U.S. government's decision to halt all military aid. This suspension includes critical defense systems such as Patriot missile batteries, which have been instrumental in countering Russian air strikes. The move, reportedly part of a broader effort to pressure Kyiv into negotiations with Moscow, signals a potential shift in U.S. strategic priorities and raises concerns about Ukraine's long-term military resilience.

The immediate consequence of this decision has been a heightened sense of urgency within Europe, where governments are now accelerating independent procurement and defense initiatives. The UK has recently pledged \$2 billion in additional weapons deliveries, while France, Germany, and Poland are ramping up their own supply commitments. However, despite these efforts, the reality remains that Europe alone lacks the industrial scale to replace the level of support previously provided by the U.S. This shortfall underscores the need for sustained investment in European defense production capabilities.

Meanwhile, tensions in the Indo-Pacific continue to escalate. China has intensified military exercises near Taiwan, prompting the U.S. Congress to review a \$10 billion weapons package for Taipei. The strategic imperative to deter Chinese aggression has led to increased naval deployments and enhanced missile defense coordination between the U.S., Japan, and Australia. This shift reinforces the growing demand for autonomous defense systems, space-based surveillance, and cyber resilience, areas where private sector innovation is increasingly driving defense modernization.

At the same time, instability in the Middle East persists, with Iran-backed proxy forces expanding operations across multiple conflict zones. The recent escalation of drone and missile attacks on U.S. and allied assets has reinforced the need for advanced missile defense systems, electronic warfare capabilities, and next-generation intelligence platforms. As security threats continue to multiply, Western governments are accelerating efforts to modernize their defense postures, enhance supply chain resilience, and strengthen military-industrial capacity.

4. Structural Investment Themes: The Case for Defense Technology Investment

The reordering of global defense priorities is not a temporary shift but a fundamental restructuring of capital allocation towards national security, supply chain independence, and next-generation defense capabilities. As traditional defense primes navigate procurement challenges and industrial bottlenecks, emerging technology-driven players are increasingly capturing market share.

Governments are recognizing the limitations of legacy defense contractors, which have struggled with cost overruns, supply chain disruptions, and slow innovation cycles. As a result, military planners are increasingly shifting procurement focus toward AI-driven intelligence systems, cybersecurity solutions, and autonomous technologies. The rise of European defense AI startups, such as Helsing, signals a shift towards integrating commercial technology into military applications. The potential for startups to gain market share is now greater than ever, as European governments seek to expand their defense-industrial base beyond traditional primes.

The role of private capital in driving innovation has never been more critical. Defense ministries are actively seeking alternative procurement mechanisms, including direct engagement with private equity and venture-backed companies, to accelerate the deployment of mission-critical technologies. This shift represents a generational opportunity for investors focused on next-generation defense capabilities.

Conclusion

The past several weeks have reinforced the reality that sovereign resilience and defense investment are no longer optional – they are essential. Governments are actively reshaping procurement strategies, expanding defense budgets, and prioritizing supply chain security. For investors looking beyond short-term public market fluctuations, the opportunity to participate in the long-term transformation of defense technology has never been stronger.

BOKA Capital remains committed to identifying and investing in the most strategically positioned deep technology companies driving this evolution.

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